

BANK INDONESIA REGULATION
Number: 8/2/PBI/2006
CONCERNING
AMENDMENT TO BANK INDONESIA REGULATION
NUMBER 7/2/PBI/2005 CONCERNING ASSET QUALITY RATING FOR
COMMERCIAL BANKS

THE GOVERNOR OF BANK INDONESIA,

- Considering:
- a. whereas in the course of their business, banks must manage credit risk and minimize potential loss by maintaining asset quality and forming adequate allowance for asset losses;
 - b. whereas to maintain asset quality and form adequate allowance for asset losses, banks classify asset quality under the approach of classification by the same asset quality for earning assets used to finance any single debtor or project (uniform classification), whether extended by 1 (one) bank or more than 1 (one) bank;
 - c. whereas by reason of the current economic conditions and to safeguard the bank role in operation of the intermediary function, a transition is necessary in the application of uniform classification;
 - d. now therefore pursuant to the considerations referred to in letter a through letter c, it is necessary to amend the Bank Indonesia Regulation concerning Asset Quality Rating For Commercial Banks;

- In view of:
1. Act Number 7 of 1992 concerning Banking (State Gazette of the Republic of Indonesia Number 31 of 1992, Supplement to the State Gazette of the Republic of Indonesia Number 3472), as amended by Act Number 10 of 1998 (State Gazette of the Republic of Indonesia Number 182 of 1998, Supplement to the State Gazette of the Republic of Indonesia Number 3790);
 2. Act Number 23 of 1999 concerning Bank Indonesia (State Gazette of the Republic of Indonesia Number 66 of 1999, Supplement to the State Gazette of the Republic of Indonesia Number 3843) as amended by Act Number 3 of 2004 (State Gazette of the Republic of Indonesia Number 7 of 2004, Supplement to the State Gazette of the Republic of Indonesia Number 4357);
 3. Bank Indonesia Regulation Number 7/2/PBI/2005 concerning Asset Quality Rating For Commercial Banks (State Gazette of the Republic of Indonesia Number 12 of 2005, Supplement to the State Gazette of the Republic of Indonesia Number 4471);

HAS DECREED:

To enact: THE BANK INDONESIA REGULATION CONCERNING AMENDMENT TO BANK INDONESIA REGULATION NUMBER 7/2/PBI/2005 CONCERNING ASSET QUALITY RATING FOR COMMERCIAL BANKS.

Article I

A number of provisions in Bank Indonesia Regulation Number 7/2/PBI/2005 concerning Asset Quality Rating For Commercial Banks (State Gazette of the Republic of Indonesia Number 12 of 2005, Supplement to the State Gazette of the Republic of Indonesia Number 4471) are amended as follows:

1. The provisions of Article 5 are amended to read as follows:

Article 5

- (1) Banks are required to apply uniform classification to Earning Assets used to finance 1 (one) debtor.
- (2) Uniform classification of Earning Assets as referred to in paragraph (1) shall also apply to Earning Assets used to finance the same project.
- (3) In the event of differences in classification of Earning Asset quality as referred to in paragraph (1) and paragraph (2), the quality of each Earning Asset shall conform to the lowest Earning Asset quality.
- (4) The provision referred to in paragraph (3) may be waived if the Earning Assets are classified on the basis of different assessment factors.

2. The provisions of Article 6 are amended to read as follows:

Article 6

- (1) Uniform classification of Earning Assets as referred to in Article 5 paragraph (1) and paragraph (2) shall also apply to Earning Assets extended by more than 1 (one) Bank and used to finance the same 1 (one) debtor or project.
- (2) The provision referred to in paragraph (1) shall also apply to:
 - a. Earning ...

- a. Earning Assets extended by each Bank in an amount greater than Rp 500,000,000.00 (five hundred million rupiahs) to the same 1 (one) debtor or project; and/or
 - b. Earning Assets extended to the same 1 (one) debtor or project on the basis of a joint financing agreement.
- (3) In the event of difference in classification of Earning Asset quality as referred to in paragraph (1) and paragraph (2), the classification by each Bank of the Earning Assets shall conform to the lowest Earning Asset quality.
- (4) The definition of lowest Earning Asset quality as referred to in paragraph (3) excludes:
- a. quality of Earning Assets classified using the additional factor of the country risk of the Republic of Indonesia; and/or
 - b. quality of Earning Assets subject to claim write-off.
- (5) The provision referred to in paragraph (3) may be waived if the Earning Assets are classified on the basis of different assessment factors.

3. The provisions of Article 7 are amended to read as follows:

Article 7

- (1) Banks are required to adjust the classification of Earning Assets quality as referred to in Article 6 at least every 3 (three) months, namely for the positions at the end of March, June, September, and December.
- (2) Banks are required to submit written information and explanations to Bank Indonesia in the event of any difference in classification of Earning Assets quality arising from the factor referred to in Article 6 paragraph (4) letter a.

- (3) The written information and explanation referred to in paragraph (2) shall be submitted to Bank Indonesia no later than the 13th (thirteenth) day of the month after the position of the required adjustment of assessment as referred to in paragraph (1) at the following addresses:
- a. the relevant Directorate of Bank Supervision, Jl. MH. Thamrin No. 2, Jakarta 10110, for a Bank having its head office in the working area of the Bank Indonesia Head Office;
 - b. the local Bank Indonesia Regional Office, for a Bank having its head office outside the working area of the Bank Indonesia Head Office.

4. The provisions of Article 8 are amended to read as follows:

Article 8

- (1) Classification of Earning Asset quality as referred to in Article 6 paragraph (2) letter a shall be implemented in phases.
- (2) The phases as referred to in paragraph (1) shall be determined on the basis of debtor classification and/or limit of Earning Assets at each Bank that are extended to the same 1 (one) debtor or project.
- (3) The phases referred to in paragraph (1) and paragraph (2) shall be stipulated further in a Circular Letter of Bank Indonesia.

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Article II

This Bank Indonesia Regulation shall come into force on the date of its enactment.

Enacted in Jakarta

Dated January 30, 2006

THE GOVERNOR OF BANK INDONESIA

BURHANUDDIN ABDULLAH

ELUCIDATION
TO
BANK INDONESIA REGULATION
Number: 8/2/PBI/2006
TENTANG
AMENDMENT TO BANK INDONESIA REGULATION
NUMBER 7/2/PBI/2005 CONCERNING ASSET QUALITY RATING FOR
COMMERCIAL BANKS

GENERAL REVIEW

To ensure the survival of their business, it is essential for banks to manage credit risk exposures at an adequate level and thus minimize potential loss from provision of funds. In this regard, credit risk management, including the maintenance of asset quality and formation of adequate allowance for losses, must operate effectively.

As a general rule, classification of earning asset quality uses the uniform classification approach in respect of earning assets used to finance any 1 (one) debtor or 1 (one) project, whether extended by 1 (one) bank or more than 1 (one) bank. If there is any difference in classification, the quality used shall conform to the lowest quality of the earning assets.

Nevertheless, in view of the recent turmoil in economic conditions and to sustain the role of banks in the operation of the intermediary function, a transition is needed in the application of uniform classification for earning assets extended by more than one bank, namely by phasing in the uniform classification. This phasing in shall operate on the basis of debtor classification and/or limit of the extended earning assets.

ARTICLE ...

ARTICLE BY ARTICLE

Article I

Number 1

Article 5

Paragraph (1)

Debtor in this paragraph is any natural person or business entity, comprising an entity in its own right and generating cash flow as a source of repayment of Earning Assets.

Paragraph (2)

The definition of same project includes but is not limited to any project in which:

- a. there are significant business linkages in a production process operated by several debtors. A linkage shall be deemed significant if, among others, the production process within an entity is dependent on the production process of another entity, for example, in the case of dependence for raw materials used in the production process.
- b. the cash flow of one entity will be significantly disrupted if the cash flow of the other entity is disrupted.

Paragraph (3)

Example 1:

Bank B extends investment Credit and working capital Credit facilities to debtor A. The classification by Bank B of each facility is as follows:

- a. Special Mention for the investment Credit; and
- b. Sub-Standard for the working capital Credit.

Because the Credit used in financing for 1 (one) debtor, the Earning Assets classification by Bank B for Credit extended to debtor A shall conform with the lowest quality of Earning Assets, i.e., Sub-Standard.

Example 2:

Bank B extends Credit facilities to debtor A and debtor C to be used in financing the same project, i.e., project D. The principal source for repayment of the Credit, whether for debtor A or debtor C, is cash flow generated by project D. The classification by Bank B of the Credit extended to debtor A and debtor C is as follows:

- a. Special Mention for debtor A; and
- b. Sub-Standard for debtor C.

Because the Credit is used to finance the same project, the Earning Assets classification by Bank B for the Credit extended to debtor A and debtor C shall conform with the lowest Earning Assets quality, i.e., Sub-Standard.

Paragraph (4)

Example:

Credit quality shall be classified on the basis of the factors of business prospects, debtor performance, and repayment ability.

Securities recognized at cost, on the other hand, shall be classified on the basis of the assessment factors of rating, prompt payment of coupons or other similar obligations and at maturity.

Because there are differences in the assessment factors for classification of Credit and Securities, the quality of Credit and Securities may be classified differently, even though for the same debtor or project.

Number 2

Article 6

Paragraph (1)

Example 1:

Bank B and Bank C extend Credit facilities to debtor A. Because the facilities are extended to the same debtor, the classification of the Credit facilities by both Bank B and Bank C must be the same.

Example 2:

Bank B and Bank C each extend Credit facilities to debtor D and debtor E to be used in financing the same project, i.e., project A. Because the facilities are extended to the same project, the classification of the Credit facilities both to debtor D by Bank B and to debtor E by Bank C must be the same.

Paragraph (2) ...

Paragraph (2)

Letter a

The limit as referred to in this regulation shall be calculated in respect of all facilities extended to each debtor or project, whether for individual debtors or a Debtor Group, if the Earning Assets are used to finance the same project.

Earning Assets extended by a Bank in any amount greater than Rp 500,000,000.00 (five hundred million rupiahs) to the same 1 (one) debtor or project shall not be influenced by the quality of Earning Assets extended by another Bank to the same debtor or project in any amount up to Rp 500,000,000.00 (five hundred million rupiahs), and vice versa.

Letter b

The definition of Earning Assets extended on the basis of joint financing agreements include financing structures such as syndication.

In applying uniform classification for Earning Assets extended on the basis of a joint financing agreement, there is no minimum limit. Accordingly, Earning Assets extended to the same 1 (one) debtor or project under a joint financing agreement must be classified the same quality, even if the Earning Assets extended by each Bank are equal to or less than Rp 500,000,000.00 (five hundred million rupiahs).

Paragraph (3) ...

Paragraph (3)

Example:

Bank B and Bank C extend Credit facilities to debtor A in which the classification by each Bank is as follows:

- a. Special Mention at Bank B; and
- b. Sub-Standard at Bank C.

Because the Credit is used to finance 1 (one) debtor, the classification of Earning Asset quality for Credit to debtor A shall conform to the lowest Credit quality, i.e., Sub-Standard.

Paragraph (4)

Letter a

Lower classification of Earning Assets solely by reason of use of the country risk of the Republic of Indonesia as an additional assessment factor shall not affect classification of Earning Assets extended to the same debtor or project by another Bank that are classified using assessment factors as stipulated in the applicable Bank Indonesia Regulation concerning Assessment of Earning Assets Quality for Commercial Banks. However, if the assessment of Earning Assets using the additional factor of the country risk of the Republic of Indonesia results in a higher classification compared to Earning Assets assessed under the applicable Bank Indonesia Regulation concerning Asset Quality Rating For Commercial Banks, the classification of the Earning Assets shall notwithstanding conform to the lowest

lowest ...

classification, i.e., the classification based on the assessment factors in the Bank Indonesia Regulation.

Letter b

Self-explanatory.

Paragraph (5)

Example:

Credit quality shall be classified on the basis of the assessment factors of business prospects, debtor performance, and repayment ability.

Securities recognized at cost, on the other hand, shall be classified on the basis of the assessment factors of rating, prompt payment of coupons or other similar obligations and at maturity.

Because there are differences in the assessment factors for classification of Credit and Securities, the quality of Credit and Securities may be classified differently, even though for the same debtor or project.

Number 3

Article 7

Paragraph (1)

When adjusting the classification of Earning Assets quality, Banks needs to keep special records of the changes in Earning Assets quality arising from the mechanism referred to in Article 6. Banks shall thereafter actively monitor changes in the quality of these Earning Assets of the debtor or project at other Banks.

Paragraph (2) ...

Paragraph (2)

Self-explanatory.

Paragraph (3)

If the 13th (thirteenth) day of the month falls on a Saturday, Sunday, or official holiday, the written information and explanations shall be submitted no later than the previous working day.

Number 4

Article 8

Paragraph (1)

Self-explanatory.

Paragraph (2)

“Debtor classification” is defined as including but not limited to the 50 (fifty) largest debtors of the Bank on an individual basis.

Paragraph (3)

Self-explanatory.

Article II

Self-explanatory.